Nos. 11775 and 11776.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

No. 11775

LAURA GAWECKI and COLLETTE MITRE, doing business under the fictitious name of SKYLARK CAFE & RESTAURANT,

Appellants,

vs.

GENERAL INSURANCE COMPANY OF AMERICA, a corporation,

Appellee.

No. 11776

LAURA GAWECKI and COLLETTE MITRE, doing business under the fictitious name of SKYLARK CAFE & RESTAURANT,

Appellants,

vs.

DUBUQUE FIRE AND MARINE INSURANCE COMPANY OF DUBUQUE, IOWA, a corporation,

Appellee.

APPELLANTS' OPENING BRIEF.

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APPELLANTS' OPENING BRIEF.

Statement of Pleadings and Facts Disclosing Jurisdiction of the District Court.

Laura Gawecki and Collette Mitre, doing business under the fictitious name of Skylark Cafe & Restaurant, filed two separate actions against the respective appellees for money alleged to be due them under a fire insurance contract, in the District Court of the United States, Southern

District of California, Central Division. It was alleged in each case that the District Court had jurisdiction because the controversy was of a civil nature and wholly between citizens of different states, and that the amount in controversy exceeded the jurisdictional minimum of $3,000.00, exclusive of interests and costs.

On the basis of these allegations, the District Court had jurisdiction under the provisions of 28 U. S. C. A., section 41. By stipulation of counsel, the two cases were consolidated for trial in the District Court.

Jurisdiction of Circuit Court of Appeal.

This Honorable Court has jurisdiction to review the judgment rendered in favor of the Dubuque Fire and Marine Insurance Company of Dubuque, Iowa, and the General Insurance Company of America by said District Court under the provisions of 28 U. S. C. A., section 225.

Statement of the Case.

Plaintiffs filed two separate actions against the respective defendant fire insurance companies. These cases were later consolidated for trial in the District Court, and, by stipulation heretofore filed, have been consolidated for hearing before this Court. The two complaints are identical in form and allege in substance that the plaintiffs were partners in the operation of the Skylark Cafe and Restaurant, located at 7519 Sunset Boulevard, Los Angeles, California; that the defendants issued fire insurance policies on the standard California form by which it insured the furniture, fixtures and equipment of the plaintiffs' restaurant; that on or about the 12th day of January, 1946, a fire occurred on the premises, resulting in loss and damage to the plaintiffs in the amount of $26,880.23; that

due proof of loss had been made, but that each defendant had refused to pay its ratable share of the loss. In each complaint it was alleged that, at the time the policies were issued, there was in full force and effect a chattel mortgage on the property issued by the plaintiffs to Walter J. McCormick and Edward A. Matlin, and a further lien in favor of Leo Kanner and Bertha Kanner to secure the payment of rent, and it was further alleged that agents of each defendant knew of these encumbrances at the time the insurance was issued. [Tr. p. 5.] The complaint against the Dubuque Fire and Marine Insurance Company prayed for judgment in the sum of $10,166.10; and the complaint against the General Insurance Company of America prayed for judgment in the sum of $20,388.95.

Each defendant answered the complaint addressed to it, and these answers are identical for all purposes. They admit the issuance of each policy to the plaintiffs, and that there was a fire on the premises; they deny that any agents of the defendant had any knowledge of any encumbrances on the property when the insurance was issued, and each defendant denies any liability to the plaintiffs; moreover, each answer sets up two affirmative defenses: (1) that the sole and unconditional ownership clause of the policy was violated, (2) that the chattel mortgage clause of each policy was violated. [Dubuque's Tr. pp. 11, 12; General's Tr. pp. 9-11.]

There was no dispute as to the amount of loss sustained by the plaintiffs, as it was stipulated that this amount had been determined by appraisal in accordance with each policy. [General's Tr. p. 48.]

The cases were tried by the court without a jury; the court rendered judgment for each defendant as prayed. [Dubuque's Tr. pp. 29-30; General's Tr. p. 28.]

Thereafter, the plaintiffs made a motion for a new trial and also a motion to amend the findings of fact and conclusions of law and to direct the entry of a new judgment in each case. [Dubuque's Tr. pp. 32-33; General's Tr. pp. 30-32.] Each of these motions was denied. [General's Tr. p. 32.]

Thereupon, within the time allowed by law, this appeal followed.

Summary of Appellants' Argument.

The foregoing facts raise one basic issue: Where property to be insured is encumbered at the time the insurance is written, can the insurer avoid liability for a valid claim of loss on the ground that these encumbrances violate certain provisions of the policy, when the insurer has made no inquiries of the insured regarding any encumbrances?

In submitting this question to this Court, the appellants take the position that the foregoing question must be answered in the negative and the judgment of the District Court reversed for the following reasons:

(1) Where there was no inquiry by the insurance company, the existence of a chattel mortgage on the property covered by fire insurance does not void the policy under the so-called chattel mortgage clause.

(2) Insurance contracts should be construed to protect the interests of the assured whenever possible.

(3) The cases relied on by the District Court in reaching its decision are distinguishable from the case at law on the ground that in the former the insured did something after the policy had been issued, which changed the risk which the insurer had accepted.

Specification of Errors.

Appellants hereby make the following specifications of error:

1. That the evidence is insufficient to sustain the findings of fact, conclusions of law and judgment.

2. That the trial court erred as follows:

(a) In denying appellants' motions for a new trial.

(b) In denying appellants' motions to amend the findings of fact and conclusions of law and to direct the entry of a new judgment.

Summary of Evidence.

In May, 1945, Laura Gawecki, a widow 62 years of age, purchased the Skylark Cafe and Restaurant located at 7519 Sunset Boulevard, Los Angeles, California, which she planned to operate with her daughter, Collette Mitre. Prior to this time, Mrs. Gawecki had never had any business experience of any kind whatsoever. [Tr. p. 68.] She made a down payment on the purchase and executed a chattel mortgage in favor of the vendors, Walter J. McCormick and Edward A. Matlin, to secure the payment of the balance of the purchase price. She also executed what purported to be another chattel mortgage in favor of Leo and Bertha Kanner, the owners of the building at 7519 Sunset Boulevard, to secure payment of the monthly rental.

The rent was never delinquent at any time. [Tr. p. 69.] These mortgages were on the property when the respective insurance policies, that are the basis of this action, were issued. They were recorded on August 22, 1945, shortly after the issuance of the policies.

Mrs. Gawecki contacted Miss Loraine O'Rourke, an insurance agent whom she had known for approximately 25 years, to handle the matter of fire insurance for her. Miss O'Rourke knew that the premises to be covered by fire insurance were subject to the aforementioned chattel mortgages [Tr. pp. 52-53]; indeed, sometime prior to this time, Mrs. Gawecki had published a notice of intention to mortgage in accordance with section 3440 of the Civil Code of the State of California. [Tr. p. 66.]

Miss O'Rourke was not an agent of the Dubuque Fire and Marine Insurance Company, but she was made an agent by the General Insurance Company of America on June 26, 1945, prior to issuance of the insurance in question by that company. [Tr. p. 53.]

When Mrs. Gawecki bought the restaurant, the property in question had previously been covered by several policies of fire insurance, including a policy issued by the appellee Dubuque Fire and Marine Insurance Company. [Tr. p. 54.] However, Miss O'Rourke felt that the property was overinsured so she cancelled several policies, but she decided to retain the policy written by the Dubuque Fire and Marine Insurance Company, and had it rewritten in favor of the new owner, Laura Gawecki. She also ordered another policy, the one issued by the General Insurance Company. The Dubuque policy was procured through one Meyer Pransky, a soliciting agent of that company, who discussed the property and insurance with Miss O'Rourke, and who had access to the escrow instructions of the sale to Mrs. Gawecki, which instructions contained detailed information about the encumbrances. [Tr. p. 5.] Miss O'Rourke contacted the Republic Insurance Company as regards the other policy, and, after being assured that the risk was covered, by a Mr. Sharp of that organization, she later received the policy of

insurance written by the General Insurance Company of America. She had no direct dealings with any representative of this latter insurance company at any time. Neither company made any inquiries whatsoever regarding the property or the nature of the risk, nor did they require or request a written application for insurance. The Dubuque Fire and Marine Insurance Company issued a policy of fire insurance No. 1362125 insuring the premises for $12,500.00, and received a premium of $150.61 as consideration therefor. The General Insurance Company of America issued a policy of fire insurance No. 2727-F-7909 insuring the premises for $35,000.00 and received a premium of $468.60 as consideration therefor. Miss O'Rourke turned the policies over to Mrs. Gawecki, who put them away without reading them.

On January 11, 1946, the property covered by the aforementioned insurance policies was damaged by fire in the amount of $26,880.23 [Tr. p. 21], a figure arrived at by appraisal at the request of the appellees and in accordance with the provision of these policies, which are the standard fire insurance policies required by the California Insurance Code, sections 2070 and 2071. Sometime after the fire, Mrs. Gawecki paid off the balance owing on the purchase price and got a full release from the vendors and mortgagees.

Due proof of loss was made, but the insurance companies refused to pay their respective shares of the loss on the ground that the following two provisions of the policies were violated:

(1) "Unless otherwise provided by agreement endorsed hereon or added hereto, this entire policy shall be void, . . . if the interest of the insured be other than unconditional and sole ownership. . . ."

(2) "Unless otherwise provided by agreement in writing endorsed hereon or added hereto, this company shall not be liable for loss or damage to any property insured hereunder while encumbered by a chattel mortgage, but the liability of the company upon other property hereby insured shall not be affected by such chattel mortgage."

The case was heard by Honorable Leon Yankwich of the Federal District Court for the Southern District of California, Central Division, who found for the defendant fire insurance companies on the ground that the existence of the chattel mortgages on the property when the insurance was issue voided any liability on the part of the defendants.

The Existence of a Chattel Mortgage on Property Covered by Fire Insurance Does Not Void the Policy Under the So-called Chattel Mortgage Clause, Where There Was No Inquiry by the Insurance Company.

Before examining the effect of the chattel mortgage executed in favor of the vendors to secure the payment of the balance of the purchase price, the matter of the so-called chattel mortgage to secure the payment of the rent may be quickly disposed of. It is to be remembered that the rent was never delinquent at any time. Under such circumstances, the California Supreme Court long ago held that such an instrument did not constitute such an encumbrance as would void the policy under a chattel mortgage clause. This proposition is succinctly stated in the syllabus of the case of *Raulet v. Northwestern Na-*

tional Insurance Company of Milwaukee, 157 Cal. 213, as follows:

> "A clause in a fire insurance policy on furniture, which voids the policy if the property be or become encumbered with a chattel mortgage, relates only to an ordinary chattel mortgage which in fact encumbers the property, and does not apply to a chattel mortgage in form, which is a mere security for rent or in the nature of a bond to become effective only in the case of the non-payment of rent."

This conclusion is in accordance with accepted dogma of the law of mortgages to the effect that there can be no mortgage in the absence of an outstanding obligation to support the mortgage. If the rent is not delinquent, it follows that there can, therefore, be no mortgage in the true sense of the word.

A more fundamental problem is presented by the chattel mortgage given to the vendors, as mortgagees, to secure the balance of the purchase price. This is a valid chattel mortgage, and presents the primary problem involved in this appeal: Can a fire insurance company avoid liability for a fire loss on the ground that the property insured was subject to a chattel mortgage at the time the policy was issued, where it made no inquiry of the assured as to any encumbrances on the property, or does this failure to inquire amount to a waiver of the chattel mortgage clause?

The aforementioned case of *Raulet v. Northwestern National Insurance Company, supra,* is an exhaustive examination of the law on the point and presents a comprehensive statement of the position of the California courts on the subject. Indeed, this decision is such a clear exposition of the law and the rationale behind the law that

the appellants feel compelled to quote from the case at some length, commencing on page 227 of the decision:

> "In Cooley's briefs on the Law of Insurance, page 1369, it is stated that 'Insurance policies generally contain a clause reciting that the policy shall be void if the insured's interest is other than sole and unconditional, or entire, sole, and unconditional ownership, and this is not expressed in the policy. . . . Its purpose is to prevent a party who has an undivided or contingent but insurable interest in property from appropriating to his own use the proceeds of the policy taken on the valuation of the entire and unconditional title, as if he were the sole owner, and to remove from him the temptation to perpetrate fraud and crime. It therefore follows that the clause is in most cases held to refer to the character and quality of the title—to the actual and substantial ownership, rather than to the strictly legal title. In other words, the insured's interest must be of such nature that he will sustain the whole loss if the property is destroyed.'
>
> "In *Miller v. Alliance Ins. Co. of Boston,* 7 Fed. 649, it is held that so long as the assured, under claim of right, had the exclusive use and enjoyment of the insured property, without any assertion of an adverse right or interest in it by any other person, he had the insurable interest under the sole and unconditional ownership clause. So here, the entire loss was sustained by plaintiff, and it seems to be the narrow view that would defeat the claim on the ground that within the contemplation of the policy she was not 'the sole and unconditional owner.'
>
> "In *Breedlove v. Norwich etc. Ins. Society,* 124 Cal. 169 [56 Pac. 772], it is said: 'Notwithstanding the fact, then, that plaintiff's interest in the property

was not that of a sole and unconditional owner, nevertheless she did have an insurable interest which will support her action.' However, the judgment in the Breedlove case was upheld upon the ground of waiver by the insurance company.

"In *Sharp v. Scottish Union etc. Co.,* 136 Cal. 542 [69 Pac. 253], it is held, as stated in the syllabus, that: 'Where there was no fraud, false swearing, concealment, or misrepresentation by the applicant for a policy of fire insurance which made the loss payable to a mortgagee, and the policy was written by an agent of the company, who delivered it to a representative of the mortgagee, and a full premium was paid and retained by the insurance company without offer of rescission after knowledge of the facts, and the assured person had an insurable interest in the property, though his wife was the owner of an undivided half interest therein, the policy may be enforced by the mortgagee, notwithstanding a clause that if the interest of the insured be other than unconditional, and sole ownership the policy should be void.' While, of course, the case can be differentiated from this, as the facts are somewhat dissimilar, yet it involves a stricter construction of the policy against the insurance company than what is insisted upon here by the respondent. In the Sharp case is cited with approval the following quotation from *Manchester Assurance Co. v. Abrams,* 89 Fed. 932 [32 C. C. A. 426]: 'Sound reason, as well as the weight of authority, inclines us to the view that where the assured has an insurable interest in the property, and in good faith applies for insurance upon the same, and makes no actual misrepresentation or concealment of his interest therein, and the insurance company refrains from making inquiry concerning his interest, and issues a policy to him,

and accepts and retains his premium, the company must be presumed to have knowledge of the condition of his title and to assure the property with such knowledge.'

"In the case at bar there was no actual nor constructive fraud, no intentional misrepresentation nor concealment, no inquiry on the part of the insurance company; the plaintiff was really vested with the title, the entire loss was sustained by her, and it cannot be held that the policy was void by virtue of the sole and unconditional ownership clause.

. . . . . .

"The question arising from the chattel mortgage is less free from difficulty. The provision in the policy as to that is: 'This entire policy, unless otherwise provided by agreement indorsed hereon or added hereto shall be void . . . if the subject of insurance be personal property and be or become encumbered with a chattel mortgage.' There is also the general provision that 'This policy is made and accepted subject to the foregoing stipulations and conditions,' etc.

"There was in fact a chattel mortgage upon the property to secure the payment of the rent for the building, but the court found in relation thereto 'That the said instrument executed by plaintiff and her husband to the said Aronson was not a chattel mortgage within the meaning of defendant's policy; that at no time from the date said instrument was executed was there any rent overdue from the lessees above named; that at no time was said instrument considered by said plaintiff as a chattel mortgage; that when the plaintiff applied, through the said George Quarre, to defendant for insurance on the said property, no inquiries were made by the said

defendant as to whether or not the said property was encumbered by a chattel mortgage, nor were any representations made by the said Quarre as plaintiff's agent, to the effect that the property was not so encumbered; that the provision in defendant's policy relating to chattel mortgages was not a material part of said policy.' The conclusion is therefrom drawn that there was no violation of this provision of the policy and 'that said defendant waived the last-mentioned clause by its conduct when application was made therefor; and that defendant is estopped by its own acts from now setting up the said clause as a defense to plaintiff's claim in this action.' . . .

"We think, however, that under the circumstances it should be held that this provision in the policy was waived by the conduct of defendant.

"There was no written application for the insurance, and, as we have seen, no actual fraud and no intentional misrepresentation by plaintiff. She was ignorant of this provision in the policy, which was secured by her agent, and no inquiry was made by the company as to the existence of any chattel mortgage.

"It must be presumed, ordinarily, that persons are familiar with the terms of written contracts to which they are parties, and in the absence of fraud they are justly bound by the provisions therein, but the rule should not be strictly applied to insurance policies. It is a matter almost of common knowledge that a very small percentage of policy-holders are actually cognizant of the provisions of their policies and many of them are ignorant of the names of the companies issuing the said policies. The policies are prepared by the experts of the companies, they are highly technical in their phraseology, they are complicated and

voluminous—the one before us covering thirteen pages of the transcript—and in their numerous conditions and stipulations furnishing what sometimes may be veritable traps for the unwary. The insured usually confides implicitly in the agent securing the insurance, and it is only just and equitable that the company should be required to call specifically to the attention of the policy-holder such provisions as the one before us.

"The courts, while zealous to uphold legal contracts, should not sacrifice the spirit to the letter nor should they be slow to aid the confiding and innocent. The defendant should either have made inquiries in reference to the chattel mortgage, required a written application covering by question and answer all the material provisions of the policy, or have consulted the records in the recorder's office where it would have been apprised of the encumbrance.

"Considering the nature of the contract and the relation of the parties, there should be no difficulty in reaching the conclusion that this provision was waived and it therefore constitutes no bar to recovery.

"In Cooley's briefs on Insurance, page 1396, it is said: 'The authorities are far from being agreed as to the necessity of disclosure, in the absence of inquiry, when the policy contains a stipulation declaring it void if the property is encumbered, and not so represented to the insurer. It has, however, been held in numerous well-considered cases that even if the policy contains a condition declaring it to be void if the interest of the insured be not fully stated, or if the property is encumbered and not so represented, or if the subject of insurance be personal property and be encumbered by a chattel mortgage, disclosure

is not necessary, in the absence of inquiry.' And further: 'That a disclosure of encumbrances is not necessary under a condition calling for a representation as to title or interest, if not absolute in fee simple, or sole and unconditional, seems to be supported by the weight of authority.'

"In *Wright v. Fire Ins. Assoc.*, 12 Mont. 485 [31 Pac. 91], the supreme court of Montana, discussing a similar provision, says: 'According to defendant's position, only one condition of said contract of insurance was ever in force, and that was the clause providing that inasmuch as a portion of the property which defendant pretended to insure was mortgaged —a fact which existed and had not been made a condition of the agreement as negotiated—the policy was entirely void *ab initio*. If this interpretation is the proper one to be upheld by the court its result is that plaintiff negotiated for insurance on her property, truly answering to all inquiries that were made concerning it; defendant promised to place a risk upon it for a certain consideration and received $105 from plaintiff for a paper which provided that she had no insurance, and this result was not according to the negotiations, because no inquiry was made as to a mortgage. No mention was made that the company would not take a risk on mortgaged property. . . . It seems to us that it would be unjust to the insurer, as well as the assured, to put such a construction on the transaction. It would be imputing turpitude to the conduct of defendant which the transaction hardly warrants, when we consider the conduct of the parties at the time the insurance contract was made as shown by the evidence. It would be assuming that the defendant was in such case obtaining, or attempting to obtain, money of plaintiff, under unscrupulous business methods, which fall

but little short of false pretense; for it is proper, in considering the effect of defendant's negotiating insurance on property, and receiving consideration therefor, to assume that defendant's managers and agents knew that mortgages, both of real and personal property, are lawful, and that not a few exist, as shown by the public records, and further that they are fully acquainted with the conditions of the policy proposed to be issued. . . . The situation further involves the misleading of the one pretended to be insured into the belief that the property in question was insured, when in fact it was not, and thus not only so contriving as to get pay for the risk without assuming it, but doing the more grievous wrong of leading the party honestly seeking and paying for insurance into suffering the entire loss of the things proposed to be insured in the transaction. . . . We hold that under the state of facts shown, defendant by writing the insurance on said merchandise without inquiry as to the mortgage thereon did consent to take the risk on the goods under mortgage as effectually as if consent had been indorsed on the policy.'

"In *German Mut. Ins. Co. v. Niewedde,* 11 Ind. App. 624 [39 N. E. 534], it is held by the appellate court of Indiana that 'where application for insurance is orally made, and there are no questions asked concerning encumbrances and the insured is unaware that the existence of a mortgage was fatal to his insurance, the insurer will be deemed to have waived a provision for forfeiture by reason of existing encumbrances. Relying upon appellant's failure to make any inquiry, appellee depends upon the policy as an indemnity in case of loss, but when the loss comes discovers that he had no insurance. If the law requires such a holding, then our province is but to

declare it. The law, however, does not demand so inexorable adherence to the letter of the contract under all circumstances and all conditions. In quite a number of cases it has been adjudged that the failure of the company to inquire about, or call any attention to, some particular fact, operates to relieve the insured from a forfeiture which would follow his omission to disclose it, under the strict wording of his policy, although the fact was one material to the risk, but not one unusual or extraordinary,' and it is furthermore declared that in determining whether such a harsh and inequitable forfeiture clause is to be deemed waived the courts have generally applied the same liberal rule in favor of the assured as governs in the construction of the contract itself.

"In *Philadelphia Tool Co. v. British-American Assur. Co.,* 132 Pa. 236 [19 Am. St. Rep. 596, 19 Atl. 77], the supreme court of Pennsylvania treated the similar question of waiver of 'the sole and unconditional ownership clause' and it said: 'The defense now taken is that the policy is partly upon real estate and partly on personal property, for which an entire premium was paid, and that as the assured had no title to the land the policy is void as to it, and being void in part is void in whole, so that no money can now be had. This position rests on one of the almost innumerable conditions, stipulations and provisos which appear on the policy and which asserts that "if the assured is not the sole and unconditional owner of the property, or if the building stood on ground not owned in fee simple by the assured, or if the interest of the assured is not truly stated in the policy" then the policy shall be void. Is this condition applicable to the case presented on this policy? A policy of insurance, like any other contract, is to be read in the light of the circumstances that sur-

round it. This policy was issued without any application or written request describing the interest of the assured in the building. No actual representation of any sort upon the subject, oral or written, is alleged to have been made by or on behalf of the assured. We ought to assume that a policy written under such circumstances was written upon the knowledge of the representative of the insurer and intended to cover in good faith the interest which the insured had in the buildings. . . . We must also remember that this policy is to be interpreted most strongly against the company whose contract it is. Applying these principles to the question now raised, we conclude that the policy written on within the knowledge of the insurer was made in view of the facts of the case, and was intended to cover such interest in the buildings as the insured had.' It is clear that the waiver of 'the sole and unconditional ownership clause' there involved a wider departure from the letter of the policy than that of the chattel mortgage clause involves under the circumstances disclosed here in view of the fact that nothing was overdue and the property insured was of greater value than the aggregate of the fact of the policy and the sum secured by the mortgage. In line with the foregoing are decisions of the courts of Indiana, Kentucky, Montana, Nebraska, Oregon, Vermont, Virginia and Washington."

In brief, the argument of the *Raulet* case is that the rule that parties know the terms of written contracts should not be strictly applied to insurance contracts that contain numerous technical provisions, which, as a matter of common knowledge, the insured seldom knows or if he knows would not understand; that people trust the insurer's agent to protect them, and hence, there is a duty

upon the insurer to inquire and call attention specifically to such provisions or ask for written applications concerning the matters covered by such clauses; that chattel mortgages are common as the insurer well knows, and that the conduct of the insurer misleads the insured into the belief that he has protection and operates as a contrivance to get paid for a risk without assuming it. This proposition and the exact language of the *Raulet* case have been cited and applied with approval ever since the case was originally handed down.

For example, in *Kavanaugh v. Franklin Fire Insurance Co.,* 185 Cal. 307, 314, decided after the adoption of the statutory fire insurance policy, the California Supreme Court, speaking through Justice Wilbur, said:

> "While it is true that an insurance policy is a contract, it is recognized that in the decisions bearing upon the responsibility of the insurance company, the policy has been treated more as a commodity than as a contract and rules have been evolved which are not applicable to ordinary contracts. It is therefore considered that when an insurance company without any inquiry as to the character of the ownership of the insured issues a policy and receives a premium therefor, it is just to assume that the insurance company intended to cover whatever interest the insured had in the property and that the insured by accepting a policy and paying the premium had the same understanding as to the legal effect of the policy. This conclusion is based somewhat upon the fact that insurance policies are usually very lengthy and contain a great many conditions in language which is somewhat obscure to the layman, and that the insurance company, having the power to write its policy in any form and in any language it chooses, should be

> deemed to have adopted language which would fulfill the mutual intent of the parties, or if not, should be estopped from claim that its policy was void *ab initio.*"

Other jurisdictions have long recognized that the mere obtaining of an insurance policy on property does not amount to a representation that the property is not encumbered, where no inquiry or voluntary statement is made concerning encumbrances.

> *Niagara F. Ins. Co. v. Layne,* 162 Ky. 665, 172 S. W. 1090;
>
> *O'Brien v. Ohio Ins. Co.,* 52 Mich. 131, 17 N. W. 726;
>
> *Koshland v. Hartford Ins. Co.,* 31 Ore. 402.

As the Missouri court said in *Morrisons v. Tennessee M. and F. Ins. Co.* (1853), 18 Mo. 262, 59 Am. Dec. 299:

> "Insurance companies may protect themselves by inquiries in relation to these things and after filling their policies with so much detail and such minutiae of information in regard to other matters as to create the impression they are satisfied, to hold that they are not bound by their contracts, unless information of another kind is communicated by the assured, which is not sought for, would be enabling them to commit the rankest injustice."

It is settled in California that only a positive concealment of the facts as to ownership is a defense, and that where no inquiry has been made by the insurer it is assumed to have insured whatever interest the assured had

in the property when the application for insurance was made.

Dunne v. Phoenix Ins. Co. of Hartford, Conn., 113 Cal. App. 256;

Kahn v. Commercial Union Fire Ins. Co., 16 Cal. App. (2d) 42;

Bass v. Farmers' Mutual Protective Fire Ins. Co., 21 Cal. App. (2d) 26.

The logic of the cases heretofore cited applies without qualification to the case at bar. No inquiry was made nor was a written application demanded of Mrs. Gawecki. She acted in complete good faith, concealing nothing from the agents of the insurer. Miss O'Rourke, acting as the agent of one appellee, was fully aware of all the encumbrances on the property insured. When she made the arrangements for the Dubuque Fire and Marine Insurance policy to be reissued in the name of Mrs. Gawecki, Meyer Pransky, agent of the Dubuque, had access to the escrow containing this information. When that same insurance company is asked to cancel a policy of fire insurance on a given piece of property and reissue that policy on the same piece of property but in the name of another person, it is put on notice that the property has been transferred. If it chooses to insure that property without any inquiry regarding the ownership of the property, it must be deemed to have insured whatever interest the new owner has in the property and to have waived any provisions in the policy inconsistent with such a conclusion.

The same reasoning applies to the General Insurance Company. It could have ascertained the nature of Mrs. Gawecki's interest in the property insured, but it deemed such information wholly unimportant. Indeed, the General Insurance Company covered the property at the re-

quest of the Republic Insurance Company without any regard whatsoever to the nature of the risk it undertook to carry, and after a loss had been sustained this company for the first time was heard to make rumblings about "sole and unconditional ownership" and "chattel mortgages."

In short, the position of the appellees is this: We shall write insurance through soliciting agents, who have no power to waive any of the provisions of the policy. We shall not request any information from either the applicant or our agent so that no matter how much the latter might know about the risk to be covered, we cannot be held bound by such knowledge; our policies contain numerous technical conditions, all of which may be used by us by way of defense in the event that the risk we assumed works to our disadvantage, but by not making any inquiry regarding these conditions our position will be inviolate in the event that a claim is filed with us.

Such a situation is a trap for the innocent applicant who deals with his insurance agent in complete good faith. Fortunately, such is not the law of California. Indeed, in this state, even where the insurance company does make an inquiry of the applicant, it has to assume liability in the event that its agent incorrectly furnishes it with the information given by the applicant. For example, in *Bass v. Farmers' Mutual Protective Fire Ins. Co.*, 21 Cal. (2d) 26, the plaintiff was the owner of the fee to one-half of the property insured, but he owned only a life estate in the other one-half. He told this to the insurer's agent, who, however, advised the company that the applicant owned the whole fee. In holding the company liable, the court said:

> "In Cooley's briefs on the Law of Insurance, volume 3, page 2594, it is said: 'From an examina-

tion of the cases, the following propositions may be regarded as established by the weight of authority: Where the insured in good faith makes truthful answers to the questions contained in the application, but his answers, owing to fraud, mistake, or negligence of the agent filling out the application, are incorrectly transcribed, the company is estopped to assert their falsity as a defense to the policy. The act of the agent whether he is a general agent with power to issue the policies, a soliciting agent or merely medical examiner for the company, are in this respect the acts of the company, and he cannot be regarded as the agent of the insured, though it is so stipulated in the application or policy.' "

Thus, even where the insurer makes appropriate inquiries, the only obligation imposed upon the applicant is to answer truthfully the questions submitted by the soliciting agent. Whether the court regards the company as bound by the knowledge thus gleaned by the soliciting agent, or whether it simply decides that, having done all in good faith that was requested of him, the applicant has a right to assume that his interest in the property is insured, the result is the same: The insurer is held liable in the event of loss, even though certain conditions of the policy may have been violated from the outset. It is manifestly unjust to hold that the insurer's position is enhanced and that it can avoid liability if it makes no inquiries at all as to the applicant's title. The law applicable to the case at bar was tersely stated in *Sam Wong v. Stuyvesant Insurance Company,* 100 Cal. App. 109, 112, in the following language:

"Moreover defendant is in no position to set up as a defense lack of ownership or that the insured did not own the ground on which the building was

situate, as it waived objection to the form of the policy and is estopped from denying liability thereunder by issuing the policy and accepting the premiums therefor without any written application having been made by the insured, and also without any discussion having been had relative to either title to the property on which the same was situate. Plaintiff herein, as owner, had an insurable interest in the building, he being in and operating the same as a dryer. (14 Cal. Jur. 465; 14 R. C. L. 915.) Prior to the adoption of the standard form of policy in this state, it was held that where the assured had an insurable interest in the property, and without fraud, in good faith applied for insurance upon the same, and made no actual misrepresentation or concealment of his interest therein, and the insurance company made no inquiry concerning his interest, and issued a policy to him, and accepted and retained the premium, the company must have been presumed to have knowledge of the condition of the title, and to have assured the property with such knowledge. (*Raulet v. Northwestern etc. Ins. Co.,* 157 Cal. 213, 107 Pacific 292; 14 R. C. L., pp. 926-932.) After the adoption of the standard form of policy, the law of waiver and estoppel remained the same as before upon this subject. (*Kavanaugh v. Franklin Fire Ins. Co.,* 185 Cal. 307, 315, 197 Pac. 99; 14 R. C. L., p. 932.)"

Accord:

Ames v. Employers' Casualty Co., 16 Cal. App. App. (2d) 255;

Hutchings v. Southwestern Automobile Ins. Co., 96 Cal. App. 318.

An application of the law of the State of California compels a reversal of the decision of the District Court.

Insurance Contracts Should Be Construed to Protect the Interests of the Assured Wherever Possible.

The philosophy which underlies these various decisions, which apparently does violence to the law of contracts, is based upon a frank recognition of the manner in which the insured and the insurer generally meet. There is no "meeting of the minds" characteristic of the ordinary contract, and the countless conditions contained in such a policy are drafted for the benefit of the insurer, not the insured. Nevertheless, the purpose of insurance, in particular fire insurance, is quite simple: The applicant wants to be reimbursed if his property is destroyed by fire and is willing to pay a substantial premium for this protection. All jurisdictions in this country, including California, endeavor, whenever possible, to fulfill the aims of insurance, as it is understood by men in the market place. In particular, the courts abhor technical forfeitures, which have the effect of placing the insurance company in the position of having received a substantial premium for having assumed no risk. This idea was embodied in the decision of *Glickman v. New York Life Ins. Co.,* 16 Cal. (2d) 631, 634:

> "Contracts of insurance should be viewed in the light of their general objects and purposes, including the legitimate conditions prescribed by the insurer. (*Raulet v. Northwestern etc. Ins. Co.,* 157 Cal. 213.) In general, the object and purpose of insurance is to indemnify the insured in case of loss, and ordinarily such indemnity should be effectuated rather than defeated. To that end, the law makes every rational

intendment in order to give full protection to the interests of the insured. (1 Couch, Cyc. of Insurance Law, p. 402 *et seq.*) Policies of insurance create reciprocal rights and obligations, and the relationship created between the contracting parties should be characterized by the exercise of mutual good faith. (1 Couch, Cyc. of Ins. Law, p. 408; see also, McElroy v. British America Assurance Co., 94 Fed. 990, 1000 [36 C. C. A. 615].) An insured is entitled to the protection which he buys and for which he pays substantial premiums. (Wade v. Mutual Ben. Health and Accident Assn., 115 W. Va. 694, 177 S. E. 611, 614.)"

Stated differently, the rule is:

When claims are honestly made, care should be taken to prevent technical forfeitures such as would ensue from an unreasonable rule of enforcement unrelated to the merits.

Grant v. Sun Indemnity Co., 11 Cal. (2d) 438;

Glickman v. New York Life Ins. Co., 16 Cal. (2d) 626;

13 Appleman, Insurance Law and Practice (1943), Sec. 7385, p. 37.

See

New York Life Ins. Co. v. Eggleston, 96 U. S. 572, 577;

Kansas City Life Ins. Co. v. Davis (C. C. A. 9), 95 F. (2d) 952, 957;

American Credit Indemnity Company v. N. K. Mitchell & Co. (C. C. C. A. 3), 78 F. (2d) 276, 277-278;

Langmaid, *Waiver and Estoppel in Insurance Law,* 20 Cal. L. Rev. 1, 40-41;

7 Univ. of Pitt. L. Rev. 148-150.

It is therefore the general rule that the condition alleged to have been breached must be material to the risk undertaken by the insurer before a policy of insurance will be voided. As was stated in *Goorberg v. Western Assurance Company,* 150 Cal. 510:

> "Where the warranty or condition which is broken does not affect the risk on certain items, the insurance should not be held to be ineffective as to those items. Such construction would subject the insured to a forfeiture for a cause which has no substantial relation to the interest of the insurer. The purpose of the warranties and conditions is to protect the insurer from liability on risks which he would have been unwilling to take for the stipulated premium, or, perhaps for any premium. And if, as to any item, the breach of condition or warranty does not at all affect the risk, the release of the insurer from liability from that item may fairly be said not to have been within the reason for the condition or warranty and hence not within the contemplation of the parties. . . . 'In other words, it is in their relation to the moral hazard that the materiality of statements as to title or interest rests.' 2 Cooley, Briefs on Ins. 1340."

In 1830, in *Strong v. Manufacturers' Ins. Co.,* 10 Pick. (Mass.) 40, 20 Am. Dec. 507, in discussing the effect of the failure of an insurer to disclose the existence of a mortgage on the property sought to be insured, in answer to the contention that a fair and full representation of interest was not made, the court said:

> "We do not perceive how the encumbrances on the plaintiff's property could be considered as material to the risk. The destruction of the house did not extinguish the mortgage debts, so that he was interested to the amount of the value of the property insured. It was not necessary to specify in the policy that the property was under mortgage. We are therefore of the opinion that here was a fair and full representation of every circumstance material to the risk."

This language is of equal validity today. The existence of the chattel mortgages in question did not materially affect the risk assumed by the appellees. The appellants' interest in the property was such that they stood the entire loss by the destruction of the property. (See Cooley's Briefs on the Law of Insurance 1369.) Furthermore, this court can take judicial notice of the fact that nowadays, as a matter of routine, fire insurance companies waive the provisions of the chattel mortgage clause by an endorsement attached to the policy. This being so, the appellants fail to see any substance in the contention of the appellees that the chattel mortgage clause was material to the risk.

The Cases Relied on by the District Court in Reaching Its Decision May Be Distinguished From the Case at Bar on the Ground That in the Former the Insured Did Something After the Policy Had Been Issued, Which Changed the Risk Which the Insurer Had Accepted.

In reaching his decision, Judge Yankwich regretfully took the position that he was powerless to aid the appellants because of the authority of the case of *Hargett v. Gulf Ins. Co.,* 12 Cal. App. (2d) 449. In that case there were no encumbrances on the property when the policy was issued. However, some time *after* the policy had been issued, the assured executed a chattel mortgage on the insured property. Later, the property was destroyed by a fire. The court held that in giving this chattel mortgage, the plaintiff violated the provisions of the policy and could not recover for the loss in the absence of an endorsement to the effect that the insurer was willing to continue the policy in force. Three things are significant in this decision:

1. The leading case of *Raulet v. Northwestern etc. Ins. Co., supra,* a comprehensive analysis of the law pertaining to the problem before the court, was not cited or referred to by the California District Court of Appeal.

2. Notwithstanding the fact that the decision in the *Hargett* case was inconsistent with the *Raulet* case, no petition for a rehearing in the District Court of Appeal was ever filed.

3. The *Hargett* case, and the cases cited by the court in that decision, all involved factual situations where the insured breached the conditions of the policy *after* it had been issued.

Assuming for the sake of argument that the existence of a chattel mortgage on insured property materially affects the risk assumed by the insurance company—this assumption is implicit in the contention of the appellees—it is of fundamental importance to notice that, in the *Hargett* case, the insured did something *after* the policy had been issued, which materially affected the risk; whereas, in the case at bar and in the *Raulet* case, the risk assumed by the insurance company remained constant from the time the policy was issued until the fire. While the cases are thus distinguishable on their facts, they can be reconciled. The *Raulet* case, which is determinative of the case at bar, holds that where the insurer makes no inquiry as to the existence of any encumbrances on the insured property, it is deemed to have insured whatever interest the insured had *at the time the policy was issued* and to have waived any provisions in the policy inconsistent with that proposition. The *Hargett* case decides, quite sensibly, that the waiver concept of the *Raulet* case should not be extended to apply to a situation in which the insured does something *after* the policy has been issued which materially alters the risk originally insured.

The facts of *Steil v. Sun Ins. Office,* 171 Cal. 795, which was the principal authority cited in the *Hargett*

case and which was also relied upon by Judge Yankwich, is equally distinguishable from the *Raulet* case and the case in issue. In that case, the insurance company insured certain goods while they were in the Chronicle Building in San Francisco. Long after the policy had been issued, the insured moved the goods to another building, where they were destroyed by fire. Quite clearly, the insurance company might not have been willing to insure the goods in the other building without a substantial increase in the premium. That is to say, the actions of the insured substantially altered the risk, after the policy had been in force, and it would be unfair to hold that the insurance company was bound to insure this new and different risk on the same terms as before.

The distinction between the *Hargett* and *Steil* cases and the *Raulet* case and the case before this court is of decisive importance; yet it was overlooked by the trial court in rendering its decision.

Conclusion.

Judge Yankwich stated that he regretted "that there is no method of compensating the plaintiffs for the undisputed loss they sustained through the fire." [General's Tr. p. 16.] Certainly the law controlling the case, as outlined above, provides not only a method, but, indeed, compels the conclusion that the appellants must be compensated by the appellees in accordance with the contracts of insurance. However, what is of equal importance is that, even if there were no such conclusive authority to sustain the appellants' position, the philosophy of the

California courts is such that where the applicant deals openly and in good faith with the insurer, the latter is held to be under a similar obligation. In effect, the insurer will be held to have provided that precise protection which by its conduct it has led the insured to believe he has purchased. The case at bar is precisely such a case.

It is therefore respectfully submitted that the judgments in favor of the Dubuque Fire and Marine Insurance Company of Dubuque, Iowa, and the General Insurance Company of America should be reversed, with instructions to enter judgment in favor of the plaintiffs.

Respectfully submitted,

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